

BEFORE THE DEPARTMENT OF COMMERCE
OF THE STATE OF MONTANA

In the matter of the adoption of New) NOTICE OF ADOPTION
Rule I pertaining to the submission)
and review of applications to the)
Treasure State Endowment Program)
(TSEP))

TO: All Concerned Persons

1. On November 21, 2007, the Department of Commerce published MAR Notice No. 8-94-62 pertaining to the public hearing on the proposed adoption of the above-stated rule at page 1853 of the 2007 Montana Administrative Register, Issue Number 22.

2. The department has adopted New Rule I (ARM 8.94.3813) as proposed, but has amended the Montana TSEP Application Guidelines dated 2008 concerning the submission and review of applications for the 2009 Legislature that are incorporated by reference in New Rule I based on comments received.

3. The department has thoroughly considered the comments received. A summary of the comments received and the department's responses are as follows:

COMMENT #1: Three comments were received in regard to the proposed limit of \$500,000 unless the applicant's proposed user rates would be 150% of the target rate, in which case \$750,000 could be requested. The first comment received stated that 150% is too high of a cut-off for a \$750,000 grant and requested that 125% be used instead. The commenter said the "real user rate number" would be higher than 150% if an applicant went for the \$750,000 amount. The second comment received stated that this proposal in essence raises the target rate, which is supposed to reflect a level of affordability, based on a community's median household income. By raising the target rate 50 percent, the rates will be more and more difficult for low and moderate income families. Increased construction costs alone warrant raising the maximum grant amount to \$750,000. Higher target rates will have a greater impact on smaller towns than on larger towns, because larger towns tend to have more large volume water and sewer rates, which raises the average without raising the impact on low-end users as much. In smaller towns without industry or business, small residential customers, often senior citizens living alone, constitute a very high percentage of the total rate users. The third comment received stated that the rationale for limiting the grant amount on just water and sewer projects is not clear because there is no similar proposed limitation for bridge construction. This suggests that bridges are more important than water, sewer, or storm drain projects and should automatically qualify for more funding. While the commenter generally agreed with limiting the grant amount, presuming it was intended to allow more applicants to obtain grant funding, it was suggested that funding levels for bridges should be reduced to \$500,000 unless extenuating circumstances exist. Another

commenter stated that the \$750,000 limit for water and sewer projects should remain unchanged, because a reduced limit of \$500,000 could dramatically affect the scope of proposed projects.

RESPONSE #1: The proposed change is in response to concerns by legislators and the administration that too few projects were being funded. This was compounded by the fact that every applicant could apply for \$750,000 regardless of where their user rates would be in relation to their target rate as long as it was above the target rate. In order to provide some additional flexibility, the department will add a third level of funding. Applicants that have proposed user rates between 125 percent and 150 percent will be eligible to request \$625,000. The second commenter stated that the target rate is being raised 50 percent, which is incorrect. The department is proposing a revision of how the target rate is calculated, which has the net effect of raising the target rate by approximately six percent, but that is a separate issue from the amount that can be applied for. Having rates high enough to qualify for the higher grant does not change the target rate. The department recognizes that construction costs have risen dramatically, and this proposal could have a greater impact on smaller communities with fewer customers to spread the cost among. Finally, target rates do not apply to bridge projects, and therefore cannot be used to distinguish between grant amounts. Furthermore, based on past applications, it is not likely that many, if any, counties would apply for the full \$750,000 due to the fact that they have limited resources for the required grant match. However, in order to be fair to all applicants, the department will modify the proposed changes to reflect that bridge projects will be limited to \$500,000 unless the applicant can clearly demonstrate that there are extenuating circumstances that exist.

COMMENT #2: A comment was received stating that the guidelines suggest that some applicants have unscrupulously set user rates artificially high to improve their scores for the TSEP grant, and in the future, they would not qualify for the additional funding of \$250,000. The commenter stated that while this "rate-jacking" practice may, in the rare occasion, happen, it would be very difficult for TSEP staff to appropriately make the determination as to what user rates should be for a given system without the benefit of a detailed rate study, which would again be "raising the bar" for the application process.

RESPONSE #2: The proposed change was added because staff has been asked in the past by applicants if it would be acceptable to raise rates to qualify for a higher grant, with the excess amount collected to be placed in reserves. This change should not be an issue for applicants as long as they can reasonably demonstrate that the proposed rates are needed to proceed with the project. Reserves are an appropriate component of the user rate, but the department expects that the reserve amount be reasonable. The department does not plan to modify the proposed change.

COMMENT #3: A comment was received in regard to a provision added that states that "the department reserves the right to modify the information submitted by the applicant in order to ensure that the projected user rate is computed properly and

most accurately reflects what the projected rate is likely to be." The commenter questioned how staff can presume that they will know how to establish a user rate for a project more appropriately than the owner of the utility.

RESPONSE #3: The proposed change is simply to provide notice that when the applicant does not properly or accurately compute the proposed user rate using the specified methodology, that the department will make changes as necessary to ensure that it is reasonably accurate. In order to compare applications equally, all applicants need to use the same methodology and apply it properly. Modifications such as this are frequently made by the department after consultation with the applicant. The department does not plan to modify the proposed change.

COMMENT #4: A comment was received that objected to the proposal that projects would need to meet start-up conditions by December 31, 2012. There are often good reasons not to meet start-up conditions by a certain deadline, including environmental, water rights, land acquisition, etc. Every project is different and this issue has not been a serious problem.

RESPONSE #4: The proposed change is in response to legislators expressing a concern about TSEP funds not being used for several years, when other projects are ready to proceed. The proposed change does include a provision that allows the department to waive the requirement if the grant recipient can demonstrate that there are extenuating circumstances beyond its control that prohibit it from completing its start-up conditions. The department does not plan to modify the proposed change.

COMMENT #5: One comment was received in regard to the proposal that would allow counties to submit one bridge application and one water or wastewater application for a preliminary engineering grant. It was requested that multiple applications should be allowed for multiple unincorporated areas.

RESPONSE #5: The department is concerned that allowing multiple applications would primarily benefit urban counties with adequate resources to submit multiple grants at the expense of more rural counties with few resources and money to submit and administer even one grant. The proposed change would already allow an additional application, which was not previously permitted. The department does not plan to modify the proposed change.

COMMENT #6: A comment was received that objected to the proposal requiring that an engineer be procured within six months if a preliminary engineering grant is awarded, and requested a longer time period, preferably nine months.

RESPONSE #6: The department is concerned about grantees not moving forward with their preliminary engineering studies in a timely manner, when there are other local governments that were unsuccessful in seeking grants for their proposed projects. Six months should be an adequate amount of time, and the proposed change does include a provision that allows the department to waive the

requirement if the grantee can demonstrate substantial progress in procuring an engineer. The department does not plan to modify the proposed change.

COMMENT #7: A comment was received regarding the clarification that the costs of the application are not eligible as a match for a preliminary engineering grant.

RESPONSE #7: Only expenses related to the preparation of the preliminary engineering report can be used for matching a preliminary engineering grant. The costs of preparing the application and the cost of the preliminary engineering report are eligible as match for a construction grant. The change in the guidelines is proposed to make this existing policy more clear. The department does not plan to modify the proposed change.

COMMENT #8: A comment was received regarding the clarification that emergency grants are not to be utilized for routine or preventative maintenance or for projects which serve as a backup for a system component. A replacement of a failed water or sewer line was used as an example of ineligibility. The commenter stated that the replacement of failed water or sewer lines is not routine, preventive, or a backup project component, but rather an unanticipated capital improvement project.

RESPONSE #8: The department agrees with the comment and will eliminate the example. However, the department will elaborate further on the clarification to point out that emergency grants are for "unforeseen events" and not for situations where a system has simply deteriorated.

COMMENT #9: Two comments were received that objected to the proposed change in scoring levels for priority #3. One commenter stated that preliminary engineering reports are the perfect tie breaker as compared to issues such as public support. The other commenter noted that the scoring weight of technical aspects of the project is being reduced with the proposed quartile scoring system, yet this part of the project application represents over 75% of the cost of preparing the application.

RESPONSE #9: The department decided to use four levels versus five levels to score priority #3, because of the difficulty in distinguishing between a good preliminary engineering report and an excellent one. This particular issue has been a major point of contention for many years with applicants, engineers, and legislators. The proposed change will allow the department to clearly distinguish between preliminary engineering reports that are adequately prepared and those that have potentially serious issues that have not been adequately addressed. The department does not plan to modify the proposed change.

COMMENT #10: Two comments were received regarding a comment attached to one of the examples of projects in the scoring of Statutory Priority #1 - specifically certain types of wastewater projects. The comment states: "The opportunities for contact with people must be documented with photos, maps, or other supporting evidence in order to demonstrate the level of public use of the area." One commenter stated that the proposal suggesting that public contact with wastewater

discharges be documented may be difficult to do. It would not be practical, for example, to wait by a stream so that people floating by can be photographed. The other commenter stated that it is difficult, if not impossible, to document a situation where someone has come in contact with wastewater. Furthermore, the requirement that wastewater projects must meet this higher level of documentation is inherently unfair. Does the program require photos and maps of people drinking water with elevated levels of contaminants? Any increased level of documentation should apply to all potential TSEP projects uniformly.

RESPONSE #10: The department is simply requesting that applicants provide as much documentation as they can, in the form of photographs primarily, so that the engineers reviewing the technical information can gain a better understanding of the area and the problem. The review engineers will probably not have the opportunity to visit the site in person and need as much insight into the nature of the area from the application in order to determine if the area is likely to be visited by the public or used for recreational purposes. For example, an aerial photo of the area obtained from the Internet accompanied by a few of regular photos from different angles is all that is being requested. The department will more clearly state in the application guidelines what is being requested from applicants based on the example provided in the previous sentence. In regard to the last comment, all projects are held to a similar level of documentation. Data regarding contaminants in drinking water, modeling of fire flow, and pictures of decayed pipe are just a few examples of documentation that may be appropriate for other types of projects.

COMMENT #11: A comment was received regarding a proposed change that encourages applicants to submit drawings, photos, etc. in electronic format to help the TSEP staff understand (visualize) the project. Is this a new scoring criterion and will failure to submit the information be cause for a reduced score? Is not the costly PER adequate documentation of a project? Undoubtedly some applicants will now prepare movies or Power Point presentations in support of their project, seeking better scores.

RESPONSE #11: The department understands the concerns expressed and will more clearly state in the application guidelines what is being requested from applicants. The department is simply looking for some of the materials already provided in the application to be submitted in an electronic format if available.

COMMENT #12: A comment was received in regard to the guidance that is provided about what is needed for a "competitive" capital improvements plan (CIP). It should be recognized that small districts cannot always afford a costly CIP, particularly when their authority is limited to water or sewer system. Also, applicants that have some type of comprehensive planning process, regardless of whether it meets the TSEP prescribed planning process, should be given some credit for their efforts.

RESPONSE #12: There are several types of comprehensive planning processes, and the TSEP ranking process does recognize and reward applicants for the range

of planning tools that can be used by communities. However, the department thinks that a CIP is the most important and appropriate tool for long-term infrastructure planning, and should be utilized whenever possible. There are grant funds to assist communities in preparing a CIP. In order for a CIP to be truly valuable, it needs to contain certain information and be used as part of the annual budget process. The department receives a wide range of CIP documents, and thinks that applicants with complete CIP documents, that are actively being utilized, should be recognized for their efforts. The department does not plan to modify the proposed change.

COMMENT #13: A comment was received that the department continues to add additional requirements for the preliminary engineering report, levels of documentation, more technical detail, etc., and the commenter encourages the department to quit "raising the bar" regarding the planning aspects of the project and focus more on the project itself. The commenter states that it is very difficult to see that the projects have benefited by this additional detail and the cost of planning has become a significant burden on small needy communities. Furthermore, the planning and grant writing expense detracts from the true financial demands of project – the cost of designing and building the facilities.

RESPONSE #13: Although the department is sensitive to the need to minimize procedural requirements for the program, the level of documentation related to certain aspects of the application, as noted by the commenter, has been increased in order for the department to be able to meaningfully distinguish between applicants and how they are scored on the seven statutory priorities. The department does not plan to modify the proposed change.

COMMENT #14: A comment was received that objected to the proposed minimum requirement of 2,700 points to be recommended for a grant, because anything that makes a project more difficult to move forward is bad.

RESPONSE #14: The Legislature funded all of the TSEP projects in 2007. The department is concerned that local governments will hastily submit an application for a project that is not well thought out or ready to proceed in hopes that the Legislature will fund all of the projects again. This provision sets a minimum standard to help eliminate those applications that are poorly prepared from being eligible for a grant. The department does not plan to modify the proposed change.

COMMENT #15: A comment was received regarding the scoring level definitions and examples that were added to the application guidelines. The commenter stated that the department should maintain some subjectivity in the process that would allow reviewers to recognize health and safety impacts. He stated that not every problem "fits into a box."

RESPONSE #15: The examples of the different kinds of projects that fit into each scoring level under Statutory Priority #1 are simply examples and are not intended to cover every scenario or unique situation. The definition of the scoring levels guides the scoring team when scoring projects. Examples are added over time as new

examples of projects arise in the scoring process, in order to assist in scoring projects. The department does not plan to modify the proposed change.

COMMENT #16: Two comments were received in regard to environmental pollution, and that there are many environmental problems that do not affect public health such as Total Maximum Daily Load (TMDL), ammonia toxicity, etc. The first comment stated that the most significant problems that communities face is satisfying environmental regulations and the commenter is concerned that environmental problems will no longer be scored high enough to be funded. The other comments, from the Department of Environmental Quality (DEQ), voiced very similar view points. To summarize, DEQ had the same concerns in regard to the scoring definitions and examples under each score level and that they do not place enough emphasis on the reduction of nutrient pollution. Furthermore, subjectivity in the ranking process could easily prevent most wastewater projects from ever reaching a level 4, while a level 5 does not appear to be achievable by the vast majority of wastewater projects.

RESPONSE #16: Solving environmental pollution problems is not included as one of the statutory purposes of the program, nor is it mentioned as part of Statutory Priority #1 ("Projects that solve urgent and serious public health or safety problems, or that enable local governments to meet state or federal health or safety standards"). Even so, the department has generally interpreted environmental pollution as a long-term indicator related to declining public health and safety. Wastewater projects have always scored equally as well as other projects, and the department thinks that they may continue to do so in the future. Over the last two application competitions, which used the same scoring level definitions, 12.5% of the wastewater projects received a level five score, 35% a level four score, and 47.5% a level three score. Comparatively, 7.5% of water projects received a level five score, 45% a level four score, and 45% a level three score. The average score given under Statutory Priority #1 for both wastewater and water projects in the last two competitions was 3.6. The department does not plan to modify the proposed change.

COMMENT #17: A comment was received in regard to a requirement that inspectors be properly trained in order to inspect and evaluate bridges. The requirement for NBI certification requires two weeks of training at an out-of-state location to become certified to rate these small simplistic bridges. Completion of the course allows persons to inspect all bridges from a short single span structure to major structures, so the commenter thinks the bulk of the course will be on longer more complex structures. If someone wants to "fudge" the numbers it is as easy to do if they are certified or not. The commenter requested that short bridges, under 20 feet, could be inspected and documented using the State Highway procedure by individuals not completing the training.

RESPONSE #17: The requirement for the NBI certification is taken from the Code of Federal Regulations. The proposal states that "inspections performed by individuals that do not meet these criteria will likely result in a lower score, or even

the minimum score, for Statutory Priority #1." The department's intent is to ensure that people are properly qualified to inspect and rate bridges, and that the bridges are properly rated. If the department thinks that the inspection and rating has been properly completed using the proper methodology and there is adequate documentation to confirm that, the department wants to have the latitude to accept the rating. The department will soften the language to "inspections performed by individuals that do not meet these criteria may result in a lower score, or even the minimum score, for Statutory Priority #1."

COMMENT #18: A comment was received in regard to the proposal that income surveys be no older than two years in order to qualify. Income surveys are a time-consuming and difficult process. If an applicant fails in their initial application, another income survey must be completed in order to apply again. This seems like an unnecessary requirement, especially for small communities where the number of households does not exceed 200. The commenter requested that a minimum frequency of four years be used instead. If necessary, the department could adjust incomes from a survey two to four years old using wage or cost adjustment factors appropriate for the area.

RESPONSE #18: The department understands that income surveys are an onerous undertaking. As such, the department agrees with the comments received and will modify guidelines accordingly. Any income survey that meets all of the TSEP requirements will be accepted so long as it was completed after the last decennial U.S. Census was taken. Income surveys older than one year will be adjusted using appropriate wage or cost adjustment factors.

COMMENT #19: A comment was received that it is not clear whether the changes will be adopted through rulemaking or if the changes are adopted only to the guidelines themselves. If the changes are adopted only to the guidelines themselves, it seems that the changes (and perhaps the guidelines themselves) would not have the effect of rules and could only be used as guidance.

RESPONSE #19: The changes to the TSEP Application Guidelines will be adopted by reference into the Administrative Rules of Montana as provided by state law. The proposed changes will be adopted through the rulemaking process and have the effect of administrative rules.

COMMENT #20: A comment was received that the commenter was pleased to see that MDOC is planning on utilizing staff engineers rather than contract engineers to review applications.

RESPONSE #20: Although not discussed in the TSEP application guidelines, the department is in the process of attempting to recruit an additional engineer so that the technical aspects of applications can be reviewed by the department's own staff rather than hiring consultants to perform that task.

COMMENT #21: A comment was received that the commenter hopes that the department adequately considers comments provided by the applicant on the department's draft technical review report. The commenter stated that the applicant's engineer has a far better understanding of the specific technical aspects of the project in comparison to a program review engineer who cannot allocate much time to learn about each project individually.

RESPONSE #21: The process of applicants reviewing the department's draft technical review report is not discussed in the TSEP application guidelines. The commenter is correct in that the applicant's engineer has a far better understanding of the project in comparison to a review engineer. However, the TSEP program has a statutory responsibility to ensure that projects solve serious health and safety problems as well as incorporate an appropriate, cost-effective technical design and provide thorough long-term solutions to the community. It is ultimately the responsibility of the department to determine the seriousness of the health and safety problems presented and assign a score that reflects the degree of seriousness. In addition, not every preliminary engineering report reviewed by the department has been adequately prepared, and some of the projects have had significant problems in terms of their technical design and proposed solutions. The department disagrees that responses by the applicant to the review engineer's comments have been ignored. There will always be differences of opinion since the evaluation process involves a great deal of judgment. Review engineers are not allowed to consider "new" information and the review engineer also has the discretion to disagree with the responses of the project engineer.

COMMENT #22: A comment was received that the added description of scoring levels is helpful.

RESPONSE #22: Comment is noted.

/s/ KELLY A. CASILLAS
KELLY A. CASILLAS
Rule Reviewer

/s/ ANTHONY J. PREITE
ANTHONY J. PREITE
Director
Department of Commerce

Certified to the Secretary of State February 4, 2008.